Supreme Court, U.S.
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No. 93-

IN THE
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1993

SHARON PRATT KELLY, *et al.*,
Petitioners,
v.
SPRINT COMMUNICATIONS COMPANY, *et al.*,
Respondents.

Petition for a Writ of Certiorari to the District of Columbia Court of Appeals

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VANESSA RUIZ
Acting Corporation Counsel

CHARLES L. REISCHEL
Deputy Corporation Counsel
Appellate Division

*EDWARD SCHWAB
Assistant Corporation Counsel

Office of the Corporation Counsel
One Judiciary Square
441 4th Street, N.W.
Washington, D.C. 20001
Tel: (202) 727-6252, Ext. 3305

**Counsel of Record*

QUESTION PRESENTED

Whether the internal consistency test enunciated in *Tyler Pipe Industries v. Washington Dept. of Revenue, 483 U.S. 232 (1987)* requires a court to invalidate a fairly apportioned state tax which confers no inherent benefits on local taxpayers simply because, if all other states adopted the same tax, some taxpayers might be encouraged to try to spread their personal property among the states in proportion to the revenues earned in each.

PARTIES

Petitioners are the District of Columbia; Sharon Pratt Kelly, Mayor of the District of Columbia; and Lorraine J. Britton, Director of the District of Columbia Department of Finance and Revenue. Respondents are Sprint Communications Company, L.P.; Cable & Wireless Communications, Inc.; Metromedia Communications Corporation; Metro Telecommunications Services, Inc.; RealCom Office Communications, Inc.; ALLNET Communication Corporation; American Telephone and Telegraph Company; AT&T Communications of Washington, D.C.; Long Distance Service of Washington, Inc.; and Mid Atlantic Telecom, Inc.

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Petition for a Writ of Certiorari
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The District of Columbia, Mayor Sharon Pratt Kelly, and Lorraine Britton, Director, Department of Finance and Revenue, petition the Court for a writ of certiorari to review a decision of the District of Columbia Court of Appeals.

OPINIONS BELOW

The March 15, 1994, decision of the District of Columbia Court of Appeals (App. 1-27) is not yet reported. The February 19, 1992, decision of the Tax Division of the Superior Court of the District of Columbia (App. 28 - 51) is not reported.

JURISDICTION

The judgment of the District of Columbia Court of Appeals was entered on March 15, 1994. The Court has jurisdiction under 28 U.S.C. § 1257(a).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Commerce Clause (Art. I, § 8, Cl.3) of the United States Constitution provides that:

> The Congress shall have Power . . . To regulate Commerce . . . among the several States . . . .

The statutes involved in this case are reproduced in the appendix. They are D.C. Law No. 7-25 (Oct. 1, 1987) and D.C. Code §§ 47-1508, 47-2005, 47-2006, and 47-2501 (Supp. 1989).

STATEMENT OF THE CASE

This case was filed by the ten long-distance telephone companies who are respondents here, to challenge the constitutionality of the District of Columbia Gross Receipts Amendment Act of 1987, D.C. Law 7-25 (A. 76 -82). The long-distance companies are in the business of selling long-distance telephone service in the District of Columbia and elsewhere. They provide interstate and international long-distance service and are precluded from providing local telephone service. *See United States v. American Telephone & Telegraph Co.*, 552 F. Supp. 131 (D.D.C. 1982), *aff'd mem.*, 460 U.S. 1001 (1983).

The 1987 law extended the gross receipts tax applicable to local telephone, gas, and electric companies, to telephone companies offering long-distance service, and it taxes gross receipts from long-distance calls which originate or terminate in the District and are locally billed. D.C. Code § 47-2501(b) (Supp. 1989). The Amendment Act was enacted in response to restructuring of the telephone industry, which left long-distance services untaxed in the District of Columbia under either the gross receipts or the sales tax. See *District of Columbia v. Chesapeake & Potomac Telephone Co.*, 516 A.2d 181 (D.C. 1986).[1/] Sales taxes and gross receipts taxes are the major District taxes on all retail business transactions conducted in the District of Columbia, and the restructuring meant that the retail sale of long-distance calls entirely escaped both taxes. *Id.*

The gross receipts tax was originally enacted by Congress in 1902; the businesses subject to it were banks, insurance companies, and gas, electric lighting, telephone, and street railroad utilities. Act of July 1, 1902, Ch. 1352, § 6, ¶¶ 5-7, 32 Stat. 619. This tax was considered a personal property tax that was measured by gross earnings; there was an exemption from *ad valorem* personal property taxation. *Id.*[2/] Congress

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[1/] Prior to the breakup of American Telephone & Telegraph Company in 1984, the District taxed most long distance business by taxing the local monopoly on its share of the receipts of AT&T's long distance business. *Chesapeake and Potomac Telephone Company* held that, after AT&T was separated from the local monopoly, the District could no longer recover receipts of long distance service by taxing on the local monopoly. See A. 32-33.

[2/] Personal property taxes on utilities and transportation companies measured by gross earnings or gross receipts were common at that time. *United States Express Co. v. Minnesota*, 223 U.S. 335, 347 (1912); L.

(continued...)

amended the law in 1939 to cover only gas, electric lighting, and telephone utilities and to tax gross receipts rather than gross earnings; it continued the personal property tax exemption. Act. of July 26, 1939, § 2, ch. 367, 53 Stat. 1107-08. This law substituted "gross receipts" for "gross earnings" because the courts had "held that 'gross earnings' means 'gross receipts' less expenditures in producing the commodity or service." H.R. Rept. No. 808, 76th Cong., 1st Sess. 6 (Jan. 9, 1939); S. Rept. 662, 76th Cong., 1st Sess. 4 (Jan. 23, 1939). The purpose of the amendment was "to tax the 'gross receipts' without the deduction for any expense." *Id.* Companies subject to the tax when the amendments were proposed to add long distance calling paid taxes at a rate of 6.7 percent of their gross receipts. D.C. Code § 47-2501 (Supp. 1989).

The 1987 law amended the gross receipts statute to cover gross receipts of long-distance telephone companies which provide service in the District. Gross receipts from long-distance calls that are billed to a District of Columbia telephone and are made from or to a District telephone are taxed. D.C. Code § 47-2501 (Supp. 1989). The amendments imposed a 6.7% tax on gross receipts beginning on September 1, 1987, payable on a monthly basis. The estimated revenue from this portion of the tax was $18.5 million per year. Report of the D.C. Council Finance and Revenue Committee on Bill No. 7-186, "Gross Receipts Amendment Act of 1987" at 10 (June 29, 1987).

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[2] (...continued)

Tribe, AMERICAN CONSTITUTIONAL LAW, § 6-19 at 464 nn. 19 & 20 (1988).

The law also provided exemptions from taxation similar to, but more limited than, the exemptions that were given to the utilities subject to the tax. The law exempts the personal property of long-distance companies used to generate receipts subject to the tax from *ad valorem* personal property taxation; property used for other purposes is not exempt. § 47-1508(a)-(3)(B). It also exempts purchases of property that will be used to generate gross receipts subject to the tax from sales and use taxes. D.C. Code §§ 47-2005(5) and 47-2206(1).[3/] These provisions also provide a credit for personal property tax paid to the District for the period of retroactivity, from July 1, 1986 to September 30, 1987.

The legislative history of the 1987 act states that the personal property and sales and use taxes exemptions were to provide the long-distance companies "equal treatment" with the gas, electric, and local telephone companies already subject to the tax and to avoid excessive taxation by allowing "the affected companies to help offset their future gross receipts tax burden." Report of the D.C. Council Finance and Revenue Committee, *supra* at 8. The legislative decision to limit the

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[3/] The exemption provisions of the 1987 act exempt, in relevant part:

> The personal property of any telecommunications company . . . used or consumed in furnishing a service if the receipts from furnishing the service are subject to a gross receipts tax in force in the District . . . [D.C. Code § 47-1508(a)(3)(B) (Supp. 1989)];
>
> Sales of property purchased by a telecommunication company . . . for use or consumption in furnishing the service or commodity are subject to a gross receipt tax or mileage tax in force in the District . . . [D.C. Code § 47-2005(5) (Supp. 1989)];
>
> Sales upon which taxes are properly collected under [District of Columbia Gross Sales Tax provisions] . . . [D.C. Code § 47-2206(1) (Supp. 1989)].

exemptions to personal property used to produce the gross receipts that are taxed was explained in the July 13, 1987, memorandum of John Wilson, Chairperson of the Committee, to other Councilmembers; he stated:

> The exemption for these [long-distance] companies will only be granted for personal property used or consumed in furnishing a service or commodity subject to a gross receipts tax.
>
> This amendment is being offered at the request of the Executive. It is felt that a rational basis exists for treating companies in the competitive marketplace in a manner different than companies which are subject to local rate regulation.[4/]

In the trial court, the long-distance companies asserted that this tax was unconstitutional under the Commerce and the Due Process Clauses because it was allegedly unfairly apportioned; discriminates against interstate commerce; and is not fairly related to services provided by the District. They also asserted that the tax violates the Due Process Clause, because it is retroactive, and because of burdens of computing the tax. The companies additionally asserted that the District does not have authority to enact tax laws, because Congress cannot delegate authority to tax, and that the tax violates the Supremacy Clause because it taxes the United States. On cross-motions for summary judgment the trial court upheld the 1987 act in all respects and rejected all of the telephone companies' challenges to the tax.

[4/] The personal property of companies providing local telephone service subject to the gross receipts tax is wholly exempt from personal property taxes. D.C. Code § 47-1508(3)(A) (1990 repl. vol.). The provision of such local service is a regulated monopoly. *See United States v. American Telephone & Telegraph Co., supra.*

The telephone companies argued that the personal property and sales tax exemptions discriminate against companies based outside the District. The trial court rejected this claim on the ground that the tax is facially neutral and treats all long-distance companies the same way. The trial court relied on the affidavit of Thomas E. Kerwin, the supervisory tax auditor assigned to monitor the long-distance companies' tax compliance, which indicated that the long-distance companies had a substantial presence in the District of Columbia; and large amounts of personal property in the District to generate long-distance services.[5/] The court stated:

> The 1987 Gross Receipts Act is facially neutral. *Every* long distance carrier owning property in the District of Columbia is subject to a personal property tax imposed by the District and *every* long distance carrier is entitled to a credit exemption to the extent that his personal property is used to produce gross receipts. Those companies who do not own property in the District are not only unable to avail themselves of the personal property exemption/credit, but they are also free from all personal property taxes in the District of Columbia. All of the Petitioners except Long Distance Services of Washington, Inc. (which leased capacity) have taken the credit in substantial amounts regarding the taxes which are the subject of the present suit for refund.

[5/] Mr. Kerwin stated that the respondent telephone companies had benefited from the personal property exemption in the following amounts during the period from July 1, 1986 through February 28, 1989:

Sprint Communications, Inc.	$802,568.00
AT&T	$652,518.00
Allnet Communications	$117,458.00
Cable & Wireless	$181,084.80
ITT	$ 60,138.00
Contel	$ 36,439.00
Starnet	$ 1,497.10

> "Such a result would not arise from impermissible discrimination against interstate commerce but from fair encouragement of in-state business." *Armco, Inc. v. Hardesty*, *supra* at 645. This credit has been preserved on the taxes against the telephone companies from the original Gross Earnings Tax of 1902 through the Toll Telecommunication Act of 1989.

(A.43-44; emphasis in original).

The respondent long-distance companies, who claimed to be based outside the District of Columbia, argued in the Court of Appeals that the personal property and sales and use tax exemptions were discriminatory because "they receive no offset against the gross receipts tax for personal property, sales, and use taxes paid to their home jurisdiction." (A. 16-17) The Court of Appeals considered it irrelevant that all of the long-distance companies operate in the District, have a substantial presence there, and have received exemptions from the District's personal property tax under the 1987 Act. (A. 22) The court also considered it irrelevant that the long-distance companies "have not yet shown that . . . they have been subjected to heavier taxation because of the taxing schemes of other jurisdictions." (A. 22)

The Court of Appeals applied the "internal consistency" test of discrimination, relying especially on *Tyler Pipe Indus. Inc. v. Washington Dep't. of Revenue*, 483 U.S. 232 (1987), and held that the tax was unconstitutional for failure to exempt all property in the District of Columbia from personal property and sales and use taxes. The Court of Appeals stated:

> The discriminatory consequences of the 1987 Act arise from the circumstance that, if the same limited exceptions existed in every state, then out-of-state carriers would pay more than in-state carriers whenever the former had property subject to their home state's per-

sonal property tax but used to produce out-of-state revenues subject to another state's gross receipts tax.

* * * *

Commerce clause discrimination arises because the 1987 Act provides only a limited exemption, or credit, to the extent that the company uses personal property in the District of Columbia to produce those receipts. As appellants hypothesize:

> A company which concentrated its property in one state but provided services in many would pay a gross receipts tax on all of its receipts and personal property tax (and sales and use taxes) on all but a small portion of its personal property. In contrast, a company which spread its property among the several states in proportion to the revenues derived therefrom--thereby becoming essentially equivalent to a "home operator" in each state--would pay a gross receipts tax but would not pay personal property taxes or sales or use tax *anywhere*.

(A. 22-23; emphasis in original).

The Court of Appeals recognized that the consequences of the adoption by all states of the District's tax were not predictable. Nevertheless, based on *Tyler Pipe*, the court stated that interference with "the 'federal free market trade unit,'" was a sufficient basis to invalidate the law. (A. 23-24) Reliance was placed on the dissenting opinion of Justice Goldberg in *General Motors Corp. v. Washington*, 377 U.S. 436, 461 (1964), where he stated:

> Nondiscrimination alone is no basis for burdening the flow of interstate commerce. The Commerce Clause "does not merely forbid a State to single out interstate commerce for hostile action. A State is also precluded

> from taking any action which may fairly be deemed to have the effect of impeding the free flow of trade between the States. It is immaterial that local commerce is subjected to a similar encumbrance."

(A. 24; citation omitted.) The court therefore held the tax unconstitutional.

Judge Farrell stated in his concurring opinion that he felt compelled by *Tyler Pipe* to join in the court's opinion. (A. 27) However, he suggested that this Court should "reexamine" the "internal consistency principle, as a test for identifying forbidden commerce clause discrimination outside the fair apportionment context." (A. 27) He believed the District tax to be reasonable as a means of preventing double taxation and expressed the view that "[b]efore the District must refund the potentially millions of dollars at stake here, it deserves a better explanation than *Tyler Pipe* provides for the invalidity of its tax scheme." *Id.*

REASONS FOR GRANTING THE WRIT

The District of Columbia and its Mayor seek review of the decision of the District of Columbia Court of Appeals which declared the Gross Receipts Amendment Act of 1987 unconstitutional under the "internal consistency" test for determining whether a tax discriminates against interstate commerce in violation of the Commerce Clause. The District's tax at issue --its tax on long distance telephone service--is non-discriminatory on its face; has not been shown to be motivated by any desire to protect local businesses against out-of-state competitors, or to have such an effect; and has no inherent tendency to protect local enterprises or to disadvantage interstate com-

merce. Furthermore, the tax was a sensible and reasonable response to the situation in the industry that it addressed.

The court of appeals believed that it was compelled to invalidate the tax because of the way the Court applied the internal consistency test in *Tyler Pipe*. We submit that *Tyler Pipe* does not require that result, because here, if the District's tax is replicated, it does not result in the protection of wholly intrastate commercial activity, as was the case there. But if *Tyler Pipe* does require that the District's 1987 tax be invalidated, then *Tyler Pipe* should be reconsidered.

The tax here has been struck down solely because of hypothetical concerns which are extremely unlikely to have any basis in reality. When a legal test becomes so divorced from its purposes (here, protecting interstate actors against actual disadvantages) and from reality, the time has come to redefine--or reconsider--the test. With respect to the "internal consistency" test, that time is now.

1. In 1987, the District of Columbia sought to tax this industry because, due to revolutionary changes in the industry, the industry had escaped virtually all D.C. taxes on businesses. See *District of Columbia v. Chesapeake & Potomac Telephone Co., supra.* When it addressed the industry in 1987, the Council used as a model the gross receipts tax enacted by Congress, as the legislature for the District of Columbia, in 1902 and 1939. That was a gross receipts tax on the gas, electric, and local telephone utilities, a congressional substitute for personal property and sales and use taxes.[6/]

[6/] Special taxes such as these, falling on a limited class of taxpayers in lieu of other taxes, have been recognized as valid under dormant Commerce Clause analysis for more than a century. *Postal Telegraph Cable Co. v. Adams*, 155 U.S. 688, 696 (1895); *Railway Express Agency, Inc. v.*

(continued...)

The Council also faced a situation where there was one very large interstate carrier headquartered in the District, MCI Telecommunications Corporation. The District had several options with respect to how to treat this situation, in which most of the long-distance carriers had substantial personal property in the District,[7/] but one of them had a great deal of personal property that had nothing to do with long distance calls to and from D.C. The Council could have provided the same full exemption for personal property and sales and use taxes provided to those already covered by the tax,[8/] or it could have eliminated the exemptions entirely. A full exemption would have greatly benefited the competitive position of MCI, by permitting it to eliminate the entire personal property tax on its headquarters operation. Eliminating the personal property exemption entirely would have opened the District to the argument that it was double-taxing long-distance services and subjecting it to more taxes than any other business activities in the District of Columbia. The Council chose a middle ground between those two. It chose to exempt personal property to the extent that the property generated the gross receipts subject to the tax. D.C. Code § 47-1508(3)(B) (Supp. 1989). *See also* 9 D.C.M.R. § 709.1(c) (1994). That alternative

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[6/] (...continued)

Virginia, 358 U.S. 434, 436 (1959). Such taxes are internally consistent because, if enacted everywhere, all taxpayers subject to the tax will pay the special gross receipts tax and none will pay the taxes replaced by the special tax.

[7/] See n.5, *supra.*

[8/] See D.C. Code § 47-1508(3)(A) (1990 repl. vol.) which wholly exempts the personal property of any gas, electric or local telephone company from personal property taxes.

seemed to avoid either undue preference or undue penalty for a carrier with a large physical presence in the District.[9/] In short, it seemed to be a fair and reasonable response to the situation the Council confronted.[10/]

2. As explained by the trial court in this case (quoted above at 7-8), the District's tax on long distance carriers is not discriminatory on its face: all long distance carriers in the District are subject to the same tax; each is entitled to an exemption from personal property taxes to the extent that its personal property generates gross receipts subject to the tax; all that have property in the District (all but one of the respondents here) have in fact realized substantial benefits from the

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[9/] A relatively large physical presence in the District ordinarily entails greater demands on local services--police and fire protection, street maintenance, waste collection, water and sewer service, and so forth--all of which sap the local treasury.

[10/] By its terms D.C. Code § 47-1508(3)(B) exempts "personal property . . . used or consumed in furnishing a service." A formula has been created to determine the amount of the exemption. The formula provides:

COLUMN (1)		COLUMN (2)		COLUMN (3)		COLUMN (4)
Current personal property tax due before column (4) credit	X	Receipts on which District gross receipts tax is paid for twelve preceding months / Gross Receipts everywhere for for twelve months preceing column (1) tax year	X	Value of personal property elsewhere July 1 of column(1) tax year / Value of property subject to District personal property tax on July 1 of column (1) tax year	=	Credit against column (1) tax NOT to exceed limits of this section

9 D.C.M.R. § 709.1(c) (1994).

exemption. *See* n.5, *supra*. The law is facially neutral, giving all the telecommunications companies subject to it to the same tax treatment; subjecting them to the same tax burdens and exemptions.

There is no evidence that this law was drafted with a discriminatory purpose or design. Instead, the evidence shows that the Council merely extended the existing tax law to the long-distance telephone companies, which, because of changes in the industry, had become untaxed. The personal property exemption generally follows the prior tax structure. Congress had traditionally exempted companies subject to the gross receipts tax from the personal property tax.[11/] As indicated, the Council's decision to limit the personal property tax exemption avoided creating too great a benefit for a company with a great deal of personal property in the District, while at the same time avoiding making this tax unduly onerous (by either historical or contemporary standards).

[11/] Historically, Congress treated the gross receipts tax as an alternative to the personal property tax. A previously indicated (n.2, *supra*), the gross receipts tax was termed a personal property tax when first enacted in 1902. It was considered appropriate to tax personal property of utility and transportation companies in this manner because "the property" of these taxpayers "being much of it of an intangible character, is difficult to reach and properly assess for taxation." *United States Express Co. v. Minnesota*, 223 U.S. 335, 347 (1912); *see also Cudahy Packing Co. v. Minnesota*, 246 U.S. 450, 455-56 (1918). A personal property tax measured by gross receipts was upheld in other cases. *Pullman Co. v. Richardson*, 261 U.S. 330, 338 (1923); *Northwestern Life Ins. Co. v. Wisconsin*, 247 U.S. 132, 138 (1918). When a personal property tax was measured by gross receipts, it was required to be in lieu of other property taxes. Otherwise, there would be a constitutionally impermissible duplication of tax burdens within the same jurisdiction. *Oklahoma (Meyer) v. Wells, Fargo & Co.*, 223 U.S. 298, 300-301 (1912); L. Tribe, AMERICAN CONSTITUTIONAL LAW § 6-19 at 464 nn. 19 & 20 (1988). The prohibition against taxing both gross receipts and personal property probably does not survive *Complete Auto Transit v. Brady*, 430 U.S. 274 (1977).

Because it is fairly apportioned, the tax does not unduly burden interstate commerce. It apportions gross receipts in the same way that the sales tax was apportioned in *Goldberg v. Sweet*, 488 U.S. 250 (1989). The tax falls on gross revenues from calls to or from the District that are billed to a District telephone. The tax meets the internal and external consistency tests for fair apportionment. *Id.* at 260-265. Since the tax is not facially discriminatory, the fact that it is fairly apportioned satisfies the "deeper meaning" of the Commerce Clause by fairly allocating "tax burdens between insiders and outsiders." *Trinova Corporation v. Michigan Department of Treasury*, 111 S. Ct. 818, 835 (1991); *Goldberg v. Sweet, supra*, at 265-266.

3. The Court of Appeals held that the tax at issue here violates the proscriptions on state action implicit in the Commerce Clause solely because it fails to meet the internal consistency standard which this Court applied to facially nondiscriminatory state taxes in *Tyler Pipe Industries, Inc. v. Washington Dept. of Taxation*, 483 U.S. 232 (1987). App. 22-24. As the Court of Appeals understood *Tyler Pipe*, that test is one in which it is imagined that the same tax is adopted in every jurisdiction and the resulting situation is then examined to determine whether there is overlapping taxation. App. 23-24. *Tyler Pipe* apparently requires "a method of taxation that eliminates all overlapping taxation"). In the Court of Appeals' view, overlaps are deemed to "impede the free flow of trade between the States" and to represent an effort "to protect the local market." App. 24 n.27 quoting Justice Goldberg's dissent in *General Motors Corp. v. Washington, supra*, 377 U.S. at 461. The court below thought that the "overlap" in this case is the absence of an exemption in District law for any personal property tax a carrier might have to

pay in another jurisdiction for personal property in that jurisdiction used to generate revenues in the District. App. 23. As the concurring judge below put it (*id.* at 27):

> Consider, for example, the carrier having property here that is used to generate telephone charges billable to an address outside the District. Those receipts fall outside the District's telecommunications tax on gross receipts; yet because another state hypothetically might capture them under its similar tax, the District must go further and exempt those receipts from the reach of its personal property or use taxes as well--either that or it must eliminate the exemption relieving locals from paying double taxes (personal property and gross receipts) based on a single transaction. Invalidating the tax was viewed as necessary to avoid a situation where a "company [might] spread its property among the several states in proportion to the revenues derived therefrom--thereby becoming essentially equivalent to a 'home operator' in each state . . . ."

App. 23 quoting the carriers' appellate brief.

4. Applying the internal consistency test to this tax unmoors the test from its purpose and from reality. This is because the telecommunications tax here has no inherent tendency to protect "home producers" and provides an uncertain basis for decisions as to where to do business. It provides unsure guidance because, even accepting the crucial "identical tax" hypothesis, obtaining optimum tax benefits depends on variables that are not fully controllable in the real world, and because actual decisions as to where to do business must take into account a multitude of considerations in addition to the costs of a single local tax.

a. The D.C. tax at issue here does not inherently tend to favor companies which have a presence in the District ("home-producers") over those which do not. That is demon-

PERCENT OF FIRM'S CALLS TAXED IN D.C.

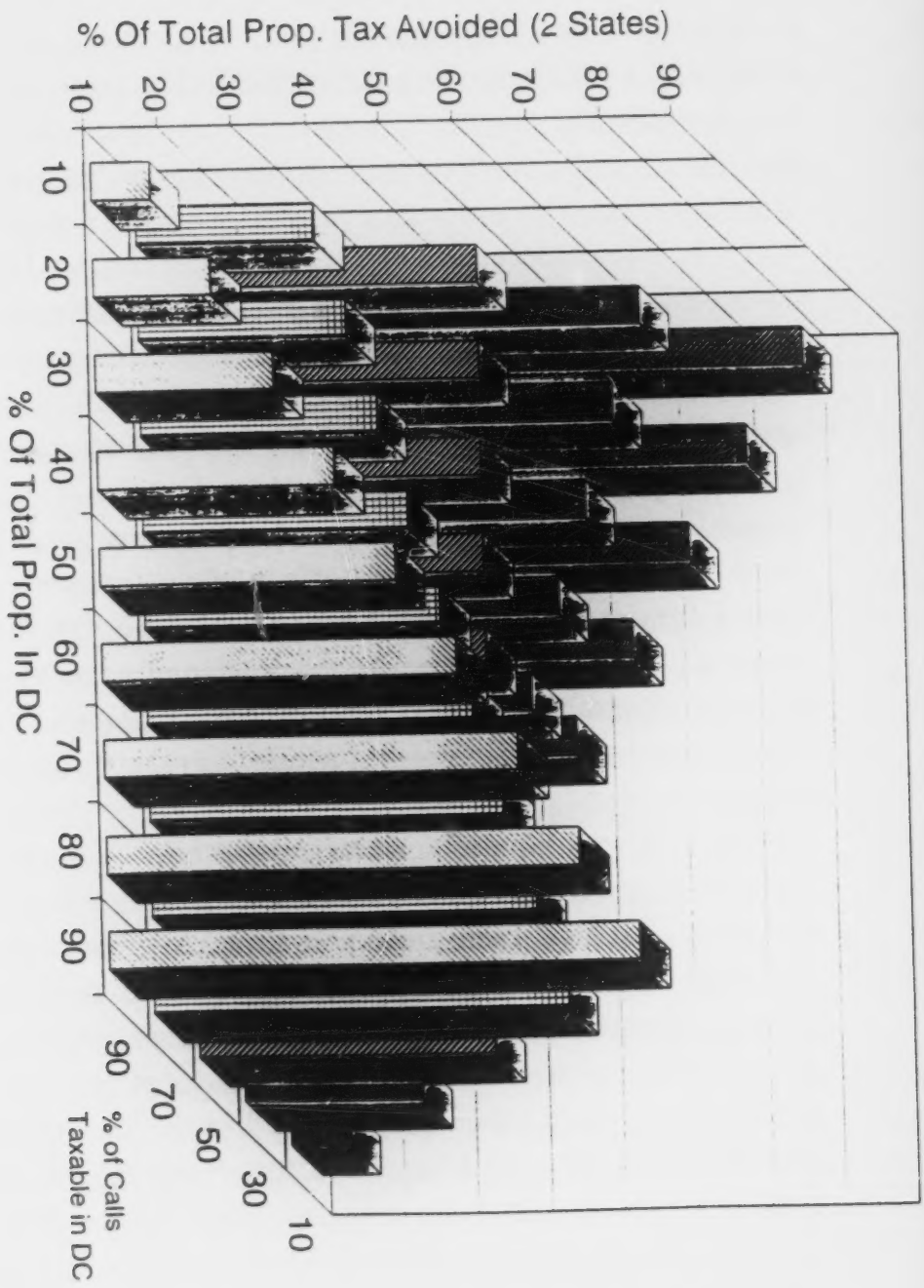
PERCENT OF TOTAL PROPERTY IN DISTRICT OF COLUMBIA

	10%	20%	30%	40%	50%	60%	70%	80%	90%
0	90 ALL MD	80 ALL MD	70 ALL MD	60 ALL MD	50 ALL MD	40 ALL MD	30 ALL MD	20 ALL MD	10 ALL MD
10%	82 1% DC 81% MD	74 2% DC 72% MD	66 3% DC 63% MD	58 4% DC 54% MD	50 5% DC 45% MD	42 6% DC 36% MD	34 7% DC 27% MD	26 8% DC 18% MD	18 9% DC 9% MD
20%	74 2% DC 72% MD	68 4%DC 64%MD	62 6% DC 56% MD	56 8% DC 48% MD	50 10% DC 40% MD	44 12% DC 32% MD	38 14% DC 24% MD	32 16% DC 16% MD	26 18% DC 8% MD
30%	66 3% DC 63% MD	62 6% DC 56% MD	58 9% DC 49% MD	54 12% DC 42% MD	52 15% DC 35% MD	46 18% DC 28% MD	42 21% DC 21% MD	38 24% DC 14% MD	34 27% DC 7% MD
40%	58 4% DC 54% MD	56 8% DC 48% MD	54 12% DC 42% MD	52 16% DC 36% MD	50 20% DC 30% MD	48 24% DC 24% MD	46 28% DC 18% MD	44 32% DC 12% MD	42 36% DC 6% MD
50%	50 5% DC 45% MD	50 10% DC 40% MD	50 15% DC 35% MD	50 20% DC 30% MD	50 25% DC 25% MD	50 30% DC 20% MD	50 35% DC 15% MD	50 40% DC 10% MD	50 45% DC 5% MD
60%	42 6% DC 36% MD	44 12% DC 32% MD	46 18% DC 28% MD	48 24% DC 24% MD	50 30% DC 20% MD	52 36% DC 16% MD	54 42% DC 12% MD	56 48% DC 8% MD	58 54% DC 4% MD
70%	34 7% DC 27% MD	38 14% DC 24% MD	42 21% DC 21% MD	46 28% DC 18% MD	50 35% DC 15% MD	54 42% DC 12% MD	58 49% DC 9% MD	62 56% DC 6% MD	66 63% DC 3% MD
80%	26 8% DC 18% MD	32 16% DC 16% MD	38 24% DC 14% MD	44 32% DC 12% MD	50 40% DC 10% MD	56 48% DC 8% MD	62 56% DC 6% MD	68 64% DC 4% MD	74 72% DC 2% MD
90%	18 9% DC 9% MD	26 18% DC 8% MD	34 27% DC 7% MD	42 36% DC 6% MD	50 45% DC 5% MD	58 54% DC 4% MD	66 63% DC 3% MD	74 72% DC 2% MD	82 81% DC 1% MD
100%	10% ALL DC	20% ALL DC	30% ALL DC	40% ALL DC	50% ALL DC	60% ALL DC	70% ALL DC	80% ALL DC	90% ALL DC

PER CENT OF PERSONAL PROPERTY TAX AVOIDED (IN HYPOTHETICAL MD & DC)
WHERE MD HAS IDENTICAL TAX AS DC (FOR DIFFERENT COMBINATIONS OF DISTRIBUTION
OF PROPERTY AND TAXABLE CALLS)

strated in the accompanying table. That table represents, in a somewhat simplified form, how the District tax operates if other jurisdictions adopt the same tax scheme. (While the table presents the situation where one other state--hypothetically, Maryland--adopts the identical tax, the same principles would hold true if any number of states adopted the D.C. tax). It shows that in those circumstances a company does *not* always benefit by increasing its presence (*i.e.*, its personal property) in the District.

In the first place, the table demonstrates that, under an identical hypothetical tax, there are two variables in each jurisdiction that determine the "optimum shelter" point for personal property (*i.e.* the point at which a firm would obtain the maximum reduction of personal property taxes in both jurisdictions combined): (1) The percentage of the firm's *business* in the District (percent of its total calls to or from D.C. and billed to the carrier in D.C.); and (2) the percentage of the carrier's *property* in the jurisdiction. In a great many circumstances, *increasing* either the company's property in the District, or its percentage of receipts in the District *decreases* the amount of personal property sheltered from personal property taxes. For example, if a carrier has 40 percent of its business in the District, increasing the percentage of its personal property in the District actually decreases the total amount of its personal property sheltered from tax in both jurisdictions combined. Thus, if 40% of its business is in D.C., by *increasing* its property from 10% to 60% in D.C., a firm *decreases* the percentage of total personal property sheltered from tax from 58% to 48%. Similarly, if a company has 40% of its personal property in D.C., *increasing* the amount of its business in D.C. from 10 percent to 60 percent *decreases* the total percentage of its personal property shel-


% Of Total Prop. Tax Avoided (2 States)
10
20
30
40
50
60
70
80
90
% Of Total Prop. In DC
% of Calls Taxable in DC

tered from tax from 58% to 48%. This is graphically illustrated at in the accompanying paragraph.[12/] The point, however, is undeniable: this tax does not inherently "favor" "home producers." Who is "favored" depends on the particular business circumstances of each individual taxpayer.

b. The consequences of a tax of this sort are not fully controllable or predictable. This is so in part because, in a competitive environment (which long distance services now are), no firm can fully control the variables that will dictate how that firm should organize to maximize its tax advantages (if that were its sole concern). Most obviously, a firm cannot control increases of its business in any competitive market; that depends in large part on the efforts of its competitors. Since a firm cannot control that key variable--and therefore cannot predict with assurance what distribution of its personal property will result in the maximum tax benefits--firms would have to base business decisions on guesses as to those consequences.

Moreover, real life decisions regarding where to do business obviously depend on much more than the consequences of a given local tax. There are almost always multiple taxes, state and local, which must be taken into account as well as a plethora of other costs--labor, travel, real estate, workers compensation, insurance, and so forth. Accordingly, the theoretical consequences of a tax scheme like the District's--even if adopted in some other jurisdictions--are unlikely to have a significant impact on how and where actual firms

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[12/] Moving from left to right on the graph implies an increase of the percentage of a firm's total property in D.C. Moving from front to back implies a decrease in the percentage of the firm's calls taxable in D.C. The height of each bar represents the total savings on personal property taxes in both jurisdictions.

choose to do business. Given their inability to control gross receipts in any jurisdiction (because of competition), and given the other considerations bearing on choices about how and where to do business, the respondents' argument that the District's tax, if replicated, will cause firms to "balkanize" their personal property is fanciful.

5. That the internal consistency test does not serve the purpose for which it is ostensibly created--to protect interstate actors from being disadvantaged relative to home state actors--is also shown by the fact that one means by which the District could meet the internal consistency test would be by arranging its taxes so that out-of-state carriers would be more severely disadvantaged. Thus, the District could satisfy the internal consistency standard by exempting from personal property taxes all personal property of carriers subject to the telecommunications gross receipts tax. However, while such a tax would be internally consistent, as interpreted by the court of appeals, it would create a substantially greater competitive "advantage" for "home producers" than the tax that was struck down because of its theoretical potential burden on interstate commerce.

6. Only truly significant risks of actual harm can justify judicial intervention invalidating a state tax law. Setting aside a state tax is a grave matter because "taxes are the life-blood of government, and their prompt and certain availability an imperious need." *Bull v. United States*, 295 U.S. 247, 259 (1935). State and local governments "chiefly rely [on taxation] to obtain the means to carry on their respective governments" and disruption of the flow of taxes "may derange the operations of government, and thereby cause serious detriment to the public." *Dows v. City of Chicago*, 78 U.S. (11 Wall.) 108, 110 (1871).

Where, as here, a state taxing scheme does not discriminate on the face of the statute, and has no inherent tendency to protect "home producers," a taxpayer who wishes to show that the taxing scheme is nevertheless discriminatory should bear a heavy burden of demonstrating that there is a real risk that interstate commerce will in fact be burdened if the tax is adopted elsewhere. *See Amerada Hess Corp. v. N.J. Taxation Div.*, 490 U.S. 66, 74-75 (1989) (An apportionment scheme cannot be invalidated "whenever it *may* result in taxation of some income that did not have its source in the taxing state"; taxpayer bears the burden of "demonstrat[ing] that there is no rational relationship between the income attributable to the state and the intrastate value of the enterprise"; quoting *Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159, 169-170, 180 (1983), and *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 272 (1978).

7. The Court should use this opportunity to clarify that *Tyler Pipe* is limited to state tax schemes that place greater burdens on interstate commercial activities than are imposed on similar intrastate activities. The District's tax does not do so. As Justice Scalia pointed out in his dissent in *Tyler Pipe* (483 U.S. at 257-258), the Court there extended the internal consistency test to state statutes that are not discriminatory on their face. *Tyler Pipe* should not be extended further.

The Court's opinion in *Tyler Pipe* pivots on the point that the tax scheme there, if adopted elsewhere, would protect wholly intrastate activity from burdens that fall on an interstate activity. Thus, the Court twice stressed that the vice of Washington State's tax scheme was that "the exemption only operates to impose a unified tax eliminating the risk of multiple taxation *when the acts of manufacturing and wholesaling are both carried out within the State*." *Id.* at 246; emphasis

added. *See also id.* at 248 ("The current B&O tax exposes manufacturing or selling activity outside the State to a multiple burden *from which only the activity of manufacturing in-state and selling in-state is exempt*" Emphasis supplied). However, if the District's telecommunications tax is replicated elsewhere, the result is not to protect wholly in-state commerce.

The District's tax scheme does not implicate wholly in-state commercial activity. It applies only to transactions that involve interstate commerce (calls to and from the District; *i.e.*, calls which necessarily cross a state line) and it affects local property taxes only because and to the extent that interstate commerce is involved. No wholly local commercial activity is implicated; it can only be made to seem so because, for tax purposes, part of this interstate activity is allocated to the District (*viz*, those interstate calls billed to the District). However, the allocation does not transform calls crossing state lines into an intrastate activity. Furthermore, as shown above, the allocation here is itself unquestionably valid under *Goldberg v. Sweet, supra.* Therefore, this is not a case like *Tyler Pipe*, in which a tax protected intrastate commerce.

At worst, the District's tax scheme, if replicated, might under some circumstances create a marginal incentive for a firm to locate personal property in jurisdictions in which it generates its receipts. But this Court has emphasized that, even when such a result is intended, "it is a laudatory goal in the design of a tax system to promote investment that will provide jobs and prosperity to the citizens of the taxing state." *Trinova Corp., supra*, 111 S. Ct. at 835. *See also Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. 318, 336-337 (1977). The Court has also been quite careful not to preclude states from providing exemptions of all sorts from personal

property taxes. *Department of Revenue of Oregon v. AFC Industries, Inc.*, 114 S. Ct. 843 (1994).[13/]

8. However, if *Tyler Pipe* requires that the internal consistency test be applied to the District's tax, the test should be reconsidered here. Justice Scalia's dissent (483 U.S. at 258-259) argues trenchantly that the internal consistency test is unsound. The test is based on the illogical premise that it is more justifiable to void a tax because of harm caused by hypothetical replication than to look at a tax's actual impact in the real world. Furthermore, the test permits and requires the courts to second-guess legislative judgments on matters that go to the very life-blood of state government without a clear risk

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[13/] The Court noted there that it is "common . . . now, as in 1976" when the statute in question was drafted, "for States with generally applicable *ad valorem* property taxes to exempt various classes of commercial property" for various "beneficial purposes." 114 S.Ct. at 850, 852. The Court listed many examples, including property tax exemptions for (a) a 10-year exemption for "new manufacturing establishments or [any] addition to an existing manufacturing establishment;" (b) "temporary exemptions of newly located or newly constructed plants, and the machinery and equipment in such plants;" (c) "business property in an 'enterprise zone';" (d) "solar energy equipment, facilities or devices" and "recycling equipment, facilities or devices;" (e) "pollution control facilities;" (f) "personal property stored in a public warehouse; and (g) "unmanufactured articles consigned for sale and held by commission merchants." *Id.* at 850, 852. A majority of states exempted "one or more classes of business personal property, including business incentives, raw materials used in textile manufacturing and allied equipment, and mechanics tools." *Id.* at 850. The Court held that "given the prevalence of property tax exemptions," congressional silence in light of other explicit prohibitions "reflects a determination to permit the States to leave their exemptions in place." *Id.* at 850.

With respect to Congressional silence, it is noteworthy here that, not only does the District legislate, as a constitutional matter, as Congress' delegate (see the Court of Appeals' decision below concerning the Origination Clause, App. 7-10), but all legislation enacted by the District's Council must lay before Congress as a precondition to its becoming law. D.C. Code § 1-233(c)(1) (1992 repl. vol.). Congress, not the Council also actually adopts the District's budget. *See* D.C. Code § 47-304 (1990 repl. vol.).

of actual harm to interstate actors. As Justice Scalia has also pointed out, *id.* at 259-260 & n.3, much of the history of the Court's prior efforts to supervise state legislation under the rubric of the Commerce Clause has been a series of debacles. Adherence to the *Tyler Pipe* internal consistency test in cases like this one seems likely to produce another.

CONCLUSION

This Court should clarify or reconsider the internal consistency test applied in *Tyler Pipe* in the context of this case. The Court should grant the petition for a writ of certiorari and reverse the decision below and hold that the 1987 District of Columbia law is a constitutionally permissible exercise of taxing authority.

Respectfully submitted,

VANESSA RUIZ
Acting Corporation Counsel

CHARLES L. REISCHEL
Deputy Corporation Counsel
Appellate Division

*EDWARD SCHWAB
Assistant Corporation Counsel

Office of the Corporation Counsel
One Judiciary Square
441 4th Street, N.W.
Washington, D.C. 20001
Tel: (202) 727-6252, Ext. 3305

**Counsel of record*